

FDIC State Profile

Summer 2004

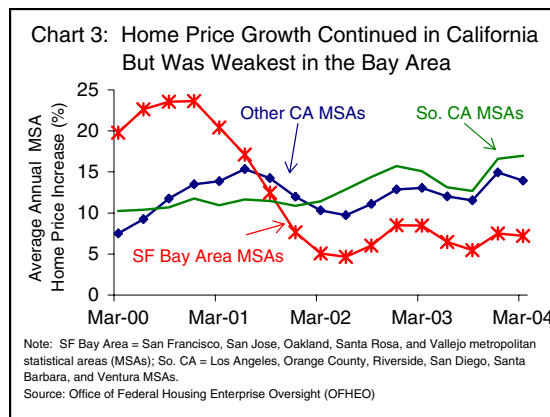
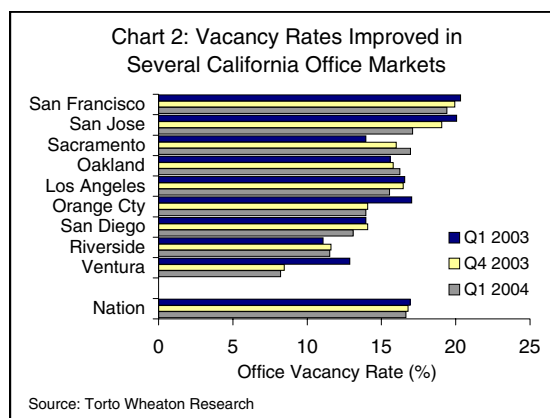
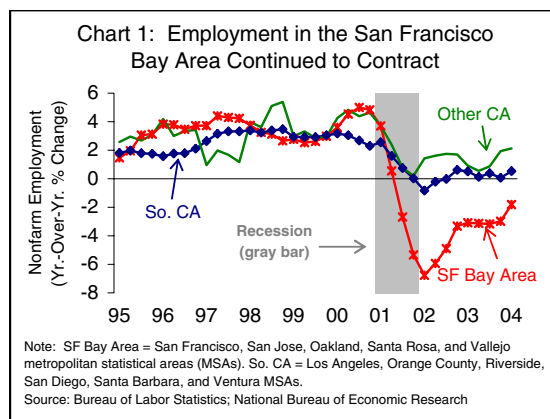
California

Employment conditions in California have started to improve, though not yet to pre-recession levels.

- Following ten consecutive quarters of year-over-year job losses, California posted a 0.3 percent year-over-year job growth rate in first quarter 2004; gains in the construction and several services sectors offset weakness in the government, manufacturing, and information industries.
- Central and rural California** reported 2.1 percent year-over-year rate during first quarter 2004 (See Chart 1)¹. In the same period, employment growth in **Southern California** finally turned positive, albeit modest, at 0.5 percent. In contrast, job losses persisted in the tech-dependent **San Francisco Bay Area**, where nonfarm employment contracted 1.8 percent year-over-year in first quarter 2004.
- Government payrolls have now contracted for four consecutive quarters. Year-over-year through first quarter 2004, California reported nearly 53,000 job losses in the government sector, with local municipalities accounting for 78 percent of combined cuts. Given that state budget problems are far from resolved, state and local government job growth will likely remain weak.

Commercial real estate (CRE) market fundamentals were weakest in the Bay Area, but CRE loan delinquencies declined.

- Office market vacancy rates showed some signs of improvement over the past few quarters; although asking rents were generally lowered to entice new office tenants. Of California's major office markets, conditions remained weakest in the **San Francisco** and **San Jose** MSAs (See Chart 2). Office asking rents in the San Francisco office market declined another 3 percent between the first quarters of 2003 and 2004, bringing the three-year total rent decline to 61 percent; in the San Jose MSA, asking rents fell another 7 percent year-over-year, pushing the three-year total decline to 63 percent.



¹Southern California includes the Los Angeles, Orange County, Riverside, San Diego, Santa Barbara, and Ventura MSAs, and the San Francisco Bay Area is defined to include the Oakland, San Francisco, San Jose, Santa Rosa, and Vallejo MSAs.

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- Sustained CRE market weakness is a concern, because the median ratio of CRE loans-to-Tier 1 capital among California-based insured institutions was 439 percent as of March 31, 2004, relatively unchanged from the year-ago level.² Despite continued CRE market softness, first quarter CRE loan delinquencies among California-based established community institutions declined year-over-year to 0.06 percent.³ Credit problems may emerge with a lag as new or renegotiated leases are signed at lower rental rates, in particular should interest rates rise.
- As of March 31, 2004, California-based insured institutions reported a median exposure to construction and development (C&D) loans of 59 percent of Tier 1 capital, more than double the median reported by insured institutions nationwide. Although median C&D exposures relative to capital declined to 44 percent among institutions headquartered in the San Francisco Bay Area, they rose modestly to 58 percent in Southern California, and to 116 percent throughout the rest of the state. Construction loan demand for residential building, which likely prompted boosted C&D loan growth, could slow should rising interest rates dampen permit activity.

Residential real estate (RRE) lenders may be vulnerable to the effects of slower home price gains.

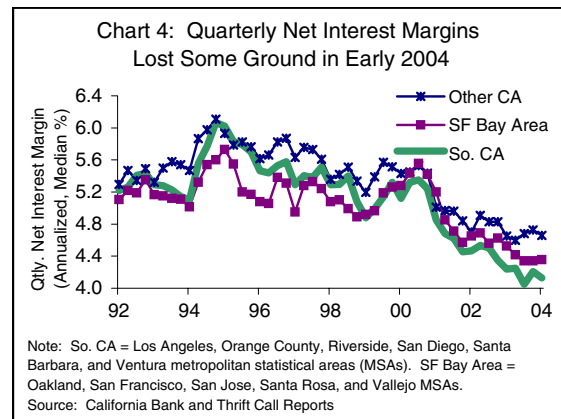
- The *Office for Federal Housing Enterprise Oversight* reported a 14 percent year-over-year increase in first quarter 2004 California home prices, the fifth fastest rate of any state. Sustained low interest rates continued to support demand and prices for homes. However, the effects of continued job weakness in the Bay Area were evident in the pattern of price appreciation across the state's major markets. Annual price appreciation averaged 7 percent among the Bay Area's MSAs versus 17 percent among Southern California's MSAs and 14 percent among the state's other MSAs (See Chart 3).
- Home price growth continued to outpace personal income gains. Only 21 percent of Californians were able to afford the median priced home as of March 2004, according to the *California Association of Realtors*. Affordability strains have become particularly pronounced in the San Francisco, Santa Barbara, Orange County, Napa, Monterey, and San Diego areas, where fifteen percent or less of households could afford the median priced home.
- Slow home price appreciation and weak employment trends in the Bay Area could signal the potential for

near-term home price declines. According to *PMI Mortgage Insurance Co.*, the probabilities of declining home values were above-average within the next two years in the San Jose (44 percent), San Francisco (19 percent), and Oakland (16 percent) MSAs.⁴

- Statewide, the first quarter 2004 median past-due 1-4 family RRE loan ratio was virtually zero. Among the state's three regions, RRE delinquency ratios tended to be highest among established community institutions based in the San Francisco Bay Area, where the median past-due RRE ratio was a very modest 0.19 percent. New loans will likely dominate RRE portfolios given high mortgage refinance activity, and credit problems could surface with additional seasoning or interest rate increases.

Quarterly net interest margin compression abated and loan delinquency ratios improved.

- The year-to-date median return on average assets (ROA) ratio was 1.03 percent in March 2004, down slightly from a year-earlier figure of 1.05 percent. Quarterly net interest income-to-average earning asset ratios contracted modestly in first quarter 2004, after improving slightly in late 2003 (See Chart 4). Modestly lower overhead and provision expense burdens contributed to ROA stability over the one-year period.
- Among insured institutions based in the state, the first quarter 2004 median past-due loan ratio was 0.50 percent, down from a year-earlier figure of 0.88 percent. Loan seasoning, diminished loan growth, or sustained economic weakness could pressure loan quality and earnings prospectively.



²CRE loans include construction, multifamily, and nonfarm-nonresidential mortgages.

³Established community institutions are defined as insured institutions in operation at least 3 years with assets of less than \$5 billion. The definition excludes industrial loan companies and specialty institutions.

⁴PMI Mortgage Insurance Co., *Economic & Real Estate Trends*, May 2004.
(http://www.pmigroup.com/lenders/media_lenders/pmi_eret04v2s.pdf)

California at a Glance

General Information	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Institutions (#)	304	317	336	348	367
Total Assets (in thousands)	746,522,249	894,664,184	808,780,280	714,813,269	616,640,985
New Institutions (# < 3 years)	44	36	34	34	37
New Institutions (# < 9 years)	90	77	73	60	58
Capital	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Tier 1 Leverage (median)	9.48	8.89	8.65	8.79	8.69
Asset Quality	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Past-Due and Nonaccrual (median %)	0.50%	0.88%	1.01%	1.19%	0.93%
Past-Due and Nonaccrual >= 5%	10	18	24	25	20
ALLL/Total Loans (median %)	1.25%	1.37%	1.41%	1.41%	1.39%
ALLL/Noncurrent Loans (median multiple)	3.05	2.80	2.74	2.53	3.02
Net Loan Losses/Loans (aggregate)	0.19%	0.29%	0.34%	0.29%	0.24%
Earnings	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Unprofitable Institutions (#)	36	31	46	32	35
Percent Unprofitable	11.84%	9.78%	13.69%	9.20%	9.54%
Return on Assets (median %)	1.03	1.05	0.99	1.03	1.02
25th Percentile	0.58	0.59	0.47	0.60	0.62
Net Interest Margin (median %)	4.39%	4.46%	4.57%	4.99%	5.25%
Yield on Earning Assets (median)	5.39%	5.84%	6.55%	8.59%	8.49%
Cost of Funding Earning Assets (median)	0.97%	1.35%	1.88%	3.65%	3.22%
Provisions to Avg. Assets (median)	0.12%	0.14%	0.18%	0.16%	0.15%
Noninterest Income to Avg. Assets (median)	0.62%	0.68%	0.67%	0.66%	0.71%
Overhead to Avg. Assets (median)	3.37%	3.40%	3.53%	3.66%	3.85%
Liquidity/Sensitivity	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
Loans to Deposits (median %)	81.62%	80.11%	79.65%	76.67%	75.59%
Loans to Assets (median %)	67.87%	67.33%	67.40%	66.63%	65.45%
Brokered Deposits (# of Institutions)	96	103	89	90	78
Bro. Deps./Assets (median for above inst.)	3.03%	3.55%	3.57%	3.00%	2.84%
Noncore Funding to Assets (median)	19.25%	20.74%	21.74%	20.65%	18.22%
Core Funding to Assets (median)	66.48%	65.59%	65.43%	66.87%	68.80%
Bank Class	Mar-04	Mar-03	Mar-02	Mar-01	Mar-00
State Nonmember	155	151	162	170	185
National	76	82	81	81	85
State Member	36	46	51	51	50
S&L	11	12	13	15	17
Savings Bank	26	26	29	31	30
Stock and Mutual SB	0	0	0	0	0
MSA Distribution	# of Inst.	Assets	% Inst.	% Assets	
Los Angeles-Long Beach CA PMSA	82	93,826,839	26.97%	12.57%	
San Diego CA	34	20,927,588	11.18%	2.80%	
Orange County CA PMSA	29	42,989,977	9.54%	5.76%	
San Francisco CA PMSA	27	180,185,407	8.88%	24.14%	
Riverside-San Bernardino CA PMSA	20	10,101,079	6.58%	1.35%	
Oakland CA PMSA	14	93,000,963	4.61%	12.46%	
Sacramento CA PMSA	13	4,874,099	4.28%	0.65%	
No MSA	12	6,086,875	3.95%	0.82%	
Stockton-Lodi CA	11	253,180,153	3.62%	33.91%	
Santa Barbara-Santa Maria-Lompoc CA	8	9,090,614	2.63%	1.22%	
San Luis Obispo-Atascadero-Paso Robles CA	7	3,434,477	2.30%	0.46%	
All Other MSAs	47	28,824,178	15.46%	3.86%	